

## **In the wind of change: Ten years of the EU consumer credit framework**

### **1. Forthcoming impact assessment of the Consumer Credit Directive**

In October 2018 the European Commission authorised a comprehensive impact assessment and an evaluation of the Directive 2008/48/EC on credit agreements for consumers (CCD).<sup>1</sup> Ten years after its adoption, the number of over-indebted households has significantly increased in most Member States (MS) of the EU.<sup>2</sup> The notion of over-indebtedness is used when individuals are unable to meet their financial obligations, which often results from consumers purchasing on credit.<sup>3</sup> Its severe economic and social consequences involve negative effects on consumption and employment as well as the adoption of austerity measures like social welfare cuts or tax increase.<sup>4</sup> Since consumer credit contracts often establish long-term obligations, involve significant amounts of money<sup>5</sup> and their terms are not understandable to consumers because of their complexity and the consumers' lack of financial literacy,<sup>6</sup> the need for a robust consumer protection framework has already been established.<sup>7</sup> The worsening trend in the consumers' financial situation indicates that the so-far adopted measures might not be effectively protecting consumers against the current challenges in the

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<sup>1</sup> Directive 2008/48/EC on credit agreements for consumers, OJ L133/66 (Consumer Credit Directive, CCD).

<sup>2</sup> Civic Consulting of the Consumer Policy Evaluation Consortium, 'The over-indebtedness of European households: updated mapping of the situation, nature and causes, effects and initiatives for alleviating its impact – Part 1: Synthesis of finding' (4.12.2013) Final report for DG SANCO, available at [www.mabs.ie/downloads/reports\\_submissions/part\\_1\\_synthesis\\_of\\_findings\\_en.pdf](http://www.mabs.ie/downloads/reports_submissions/part_1_synthesis_of_findings_en.pdf) (last accessed 29 August 2018), 5-6, 75.

<sup>3</sup> D.V. Cerini, 'Consumer Over-Indebtedness, Credit Contracts and Responsible Lending', *Global Jurist* (2017) 17(3), 1; Civic Consulting (fn 2), 150-156.

<sup>4</sup> Civic Consulting (fn 2), 197-200.

<sup>5</sup> P. Rott, 'Consumer Credit', in N. Reich et al. (eds), *European Consumer Law* (Intersentia 2014), 200.

<sup>6</sup> V. Mak, 'The Myth of the "Empowered Consumer" – Lessons from Financial Literacy Studies', *Zeitschrift für Europäisches Unternehmens- und Verbraucherrecht* (2012) 1(4), 256.

<sup>7</sup> Rott (fn 5), 204-207.

financial world. This warrants a closer look at the provisions of the CCD and the implementation, and functioning thereof, in the MS.

The CCD aims to ensure greater market competitiveness, promote confidence in the use of consumer credit, secure contract fairness and tackle over-indebtedness.<sup>8</sup> To reach these objectives, the CCD adopted a variety of preventive and corrective measures. These measures include information obligations, the principle of responsible lending, creditworthiness assessment, standardisation of cost calculation (with the introduction of the Annual Percentage Rate, APR) and information (through the adoption of the Standard European Consumer Credit Information form, SECCI), the right of withdrawal and the early repayment of credit.<sup>9</sup> What will the current evaluation of some of these measures and their implementation show?

## 2. Information obligations

Amongst the above-mentioned measures, information duties remain the main consumer protection tool used in the area of consumer credit.<sup>10</sup> The European legislator tends to believe that consumers who have received adequate information about consumer credit will knowledgeably compare credit offers available on the market.<sup>11</sup> They will make a responsible

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<sup>8</sup> Recitals 7-8 CCD. See also I. Ramsay, 'Consumer credit regulation after the fall: International dimensions', *Zeitschrift für Europäisches Unternehmens- und Verbraucherrecht* (2012) 1(1), 24-26.

<sup>9</sup> U. Reifner and I. Herwig, 'Consumer education and information rights in financial services', *Information & Communications Technology Law* (2003) 12(2), 128-129; S. Grundmann and Y.M. Atamer (eds), *Financial Services, Financial Crisis and General European Contract Law: Failure and Challenges of Contracting* (Kluwer Law International 2011), 191-192, 383, 393-395; Cerini (fn 3), 1; I. Benöhr, *EU Consumer Law and Human Rights* (Oxford University Press 2013), 116-119; Vandone is of the opinion that the Directive's objectives are aimed to be achieved through regulation of four areas – information, assessment of households' creditworthiness, rights concerning credit agreements, and creditors and credit intermediaries – see D. Vandone, *Consumer Credit in Europe Risks and Opportunities of a Dynamic Industry* (Physica 2009), 101-102.

<sup>10</sup> Recitals 19, 24, 27, 31, 32 and Articles 4-6 and 10 CCD.

<sup>11</sup> Scholars have questioned this information paradigm as consumers do not read and struggle to understand (pre-)contractual information. See e.g. O. Ben-Shahar and C. Schneider, 'The Failure of Mandated Disclosure', *University of Pennsylvania Law Review* (2011) 159(3), 649-651.

decision on a particular credit agreement<sup>12</sup> and know how to enforce their contractual rights.<sup>13</sup> The example of foreign currency loans, popular in the last two decades in many MS of Eastern and Central Europe, illustrates the importance of understandable information on credit conditions, and the consequences of concluding a consumer credit contract. Such loans lead to borrowing money in or linked to a currency that diverges from the one in which consumers receive their salaries. Consequently, it is the fluctuation of the foreign currency on the market that determines the exact amount of the payable credit. Any appreciation of the foreign currency will increase the cost of the consumer credit and since the consumer receives his or her salary in the local currency, he or she will not find relief in their income increasing simultaneously, as well. In the *Andriuciuc* case,<sup>14</sup> the European Court of Justice (ECJ) declared it insufficient for credit providers to only inform consumers of the link between the foreign and the local currencies in the calculation of the credit's amount. Instead, credit providers are expected to illustrate the risk consumers are taking when borrowing in a foreign currency, by showing them the possible variations in the exchange rate and their economic impact. The *Andriuciuc* case is just one of the recent examples of the ECJ's case law on foreign currency loans where the ECJ indicates in detail how credit providers could comply with their information obligations. Such specific guidelines are missing in the CCD and the Guidelines of the Commission.<sup>15</sup> Furthermore, the Guidelines seem to declare that the enforcement of the provision of credit information to consumers will be limited to ensuring that only formal transparency requirements have been met. Namely, they emphasise the need to provide information, which is neither lengthy nor hidden in other information, in order to enhance the information's understandability. Depending on whether national enforcement authorities followed the Commission's guidelines or the ECJ's case law, we could thus expect to find different applications of the provisions of the CCD. Such differences should highlight a need for more regulatory intervention in this area. This intervention could require credit providers to test the understandability of their disclosure on a representative sample of consumers. Moreover, it could lead to the adoption of the same toolbox, e.g. further defining requirements

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<sup>12</sup> See, e.g. Recitals 18-19 CCD; Mak (fn 6), 256; M. Schaub, 'How to Make the Best of Mandatory Information Requirements in Consumer Law', *ERPL* (2017) 25(1), 28-29; Ben-Shahar & Schneider (fn 11), 649-651.

<sup>13</sup> C. Leone, 'Transparency revisited – on the role of information in the recent case-law of the CJEU', *ERCL* (2014) 11(1), 322-325.

<sup>14</sup> *Andriuciuc and Others v Banca Românească SA* (C-186/16), ECLI:EU:C:2017:703 at [44-51].

<sup>15</sup> SWD(2012)128 final, 'Guidelines on the application of Directive 2008/48/EC in relation to costs and the Annual Percentage Rate of charge'.

for the transparent provision of information, or even standardisation.

### 3. Standardisation

One of the biggest achievements of the CCD is the introduction of a standard formula for the calculation of the credit's cost – the APR. Article 3 CCD defines the APR as 'the total cost of the credit to the consumer, expressed as an annual percentage of the total amount of credit'.<sup>16</sup> The introduction of this standard cost calculation aims to ensure a greater comparability of credit offers for consumers and to avoid deceptive cost presentation.<sup>17</sup> This, in turn, should contribute to consumers' better informed decision-making.

As behavioural studies have widely recognised that standardisation increases the disclosures' transparency,<sup>18</sup> the European legislator attempted to standardise not only the credit cost but also the provision of other information.<sup>19</sup> Under the CCD, mandatory pre-contractual information generally has to be provided through the SECCI form.<sup>20</sup> However, credit providers may give consumers additional information, as long as they issue it in a separate document, annexed to the SECCI form.<sup>21</sup> The flexibility granted to credit providers in issuing additional explanations may not be in the consumers' best interests. Scholars have identified that information overload has a negative impact on the consumers' level of understanding.<sup>22</sup> Moreover, providing consumers with other than mandatory information might distract them from the information that is most relevant for their decision-making.<sup>23</sup> The lack of form prescribed for the provision of additional information could also be questioned. If the European policymaker believes that the use of a table in the SECCI form increases the disclosure's transparency, it is surprising that credit providers are not obliged to disclose

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<sup>16</sup> The calculation details of the APR are laid down in Article 19 CCD, whilst the exact mathematical formula on the basis of which the APR is to be calculated is stipulated and explained in Annex I to the CCD.

<sup>17</sup> Recitals 18-19 CCD.

<sup>18</sup> D. Horton, 'Flipping the Script: Contra Proferentem and Standard Form Contracts', *University of Colorado Law Review* (2009) 80(2), 473; M. Faure and H. Luth, 'Behavioural Economics in Unfair Contract Terms', *JCP* (2011) 34(3), 338.

<sup>19</sup> Recitals 19 and 43 CCD.

<sup>20</sup> Article 5(1) CCD.

<sup>21</sup> *Idem*.

<sup>22</sup> Faure and Luth (fn 18), 346, 348.

<sup>23</sup> J. Davis, 'Protecting Consumers from Overdisclosure and Gobbledygook: An Empirical Look at the Simplification of Consumer-Credit Contracts', *Virginia Law Review* (1977) 63(6), 847-856.

additional information in the same manner. This difference could perhaps be explained by the varied importance of mandatory versus additional information. The European legislator might have attempted to ensure a more prominent display of mandatory information through the use of the SECCI form, as well as allowing consumers to better identify the disclosures required by law from those chosen by credit providers. However, the European policymaker does not require that the display of additional information should be less prominent than that of mandatory information. Furthermore, previous research found that consumers found the information presented in tables such as the SECCI form to be unclear and difficult to understand.<sup>24</sup> Therefore another goal of the evaluation should be to examine the effectiveness of the attempted standardisation of credit information and test whether policymakers should rely on standardisation in a more consistent manner.

#### 4. Creditworthiness assessment & responsible lending

The original proposal of the European Commission for the CCD intended to introduce the principle of responsible lending as a leading principle of consumer protection in the consumer credit framework. The principle of responsible lending would have obliged a credit provider to assess, by any means at his disposal, the creditworthiness of consumers, prior to providing them with a credit offer. This assessment would have then informed a credit advice that the credit provider issues to consumers.<sup>25</sup> Despite its potential for diminishing the consumer over-indebtedness this proposal was heavily criticised and, therefore, the final version of the CCD heavily curtailed this duty. Most importantly, the CCD did not determine the credit provider's obligations in case the consumer lacked creditworthiness.<sup>26</sup> The author expects the Commission to now re-evaluate the need to further regulate the creditworthiness assessment, its application in cross-border situations and legal consequences of a consumer's lack of

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<sup>24</sup> The Gallup Organisation, *Testing of a Standardised Information Notice for Consumers on the Common European Sales Law*, available at [http://ec.europa.eu/justice/contract/files/common\\_sales\\_law/cesl\\_gallup\\_consortium\\_final\\_report\\_en.pdf](http://ec.europa.eu/justice/contract/files/common_sales_law/cesl_gallup_consortium_final_report_en.pdf) (last accessed 29 August 2018).

<sup>25</sup> Such a creditworthiness assessment has previously been conducted in some MS, e.g. Belgium and France, see e.g.: J. Benedict, 'Responsible Lending – Das europäische Vertragsrecht zwischen *caveat emptor* und *caveat creditor*', *ZEuP* (2008), 394-410.

<sup>26</sup> Article 8(1) CCD.

creditworthiness. Perhaps, following the example of the Mortgage Credit Directive,<sup>27</sup> credit providers should only make the consumer credit available when the results of the creditworthiness assessment showed that consumers would likely meet their obligations under the credit agreement.

## 5. What to expect?

The commissioned evaluation of the CCD will be comprehensive. It will not only examine the implementation of the above-mentioned measures in all MS but also analyse the economic impact of the adoption of these measures on the credit market. As it uses mystery shopper exercises in its methodology, it may provide the additional information on the consumers' experience and identify further vulnerabilities and best practices in the credit market. We can expect it to address the applicability and suitability of the current CCD framework to protect consumers against the risks of mis-selling and over-indebtedness coming with the new forms of lending and credit providers, such as crowdfunding, fast credits, SMS loans. It should also provide an overview of the different regulatory choices made by the Member States in the non-harmonised areas, e.g., with respect of adopting caps on interest rates, supervisory requirements and sanctions. Scholars and practitioners in the consumer credit field should, therefore, pay attention in the coming months when the evaluation report is published and anticipate EU legislative actions to follow.

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<sup>27</sup> Directive 2014/17/EU on credit agreements for consumers relating to residential immovable property, OJ L60/34 (Mortgage Credit Directive), Article 18(5)(a).